



EAST KENTUCKY POWER COOPERATIVE

November 29, 2004

Ms. Elizabeth O'Donnell  
Executive Director  
Public Service Commission  
211 Sower Boulevard  
Frankfort, KY 40602

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PUBLIC SERVICE  
COMMISSION

HAND DELIVERED

Re: PSC Case No. 2004-00330

Dear Ms. O'Donnell:

Please find enclosed for filing with the Commission an original and eight (8) copies of the Reply Comments of East Kentucky Power Cooperative, Inc., Inter-County Energy Cooperative Corporation, Nolin Rural Electric Cooperative Corporation, and Salt River Electric Cooperative Corporation to the Comments of the Attorney General in this case dated November 19, 2004.

Very truly yours,

Charles A. Lile  
Senior Corporate Counsel

Enclosures

Cc: Elizabeth E. Blackford, Esq.- Office of the Attorney General

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COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

NOV 29 2004

PUBLIC SERVICE  
COMMISSION

In the matter of:

THE APPLICATION OF EAST KENTUCKY POWER, INC. )  
INTER-COUNTY ENERGY COOPERATIVE CORPORATION, )  
NOLIN RURAL ELECTRIC COOPERATIVE CORPORATION, ) Case No. 2004- 00330  
AND SALT RIVER ELECTRIC COOPERATIVE, FOR AUTHORITY )  
TO IMPLEMENT A FIXED BILL PILOT PROGRAM )

REPLY COMMENTS OF THE JOINT APPLICANTS

On August 20, 2004, East Kentucky Power Cooperative, Inc, Inter-County Energy Cooperative Corporation, Nolin Rural Electric Cooperative Corporation and Salt River Electric Cooperative (“Joint Applicants”), filed an Application for authority to implement a Fixed Bill Pilot Program. Following two rounds of discovery, the Attorney General (the "AG") filed a Request for Further Proceedings with the Public Service Commission (the "Commission") indicating that a hearing was not necessary, but requesting the opportunity to file written comments in the event a hearing was not scheduled by the Commission. In response, the Joint Applicants indicated that a hearing was not required and requested the opportunity to file reply comments to any comments filed by the AG. On November 9, 2004, the Commission issued an Order directing that any written comments from the AG be filed by November 19, 2004, and that any response comments from the Joint Applicants be filed by November 29, 2004. The Joint Applicants hereby submit the following comments in response to those filed by the AG.

**1. The AG comments that the fixed bill product is a price-based product that is not appropriate in a regulated environment, and it would be difficult, if not impossible to prevent recovery of any losses in a future rate case.**

**The Joint Applicants Respond:**

### **A. The fixed bill product has been mischaracterized as price-based**

The AG's comments begin with an assertion that the absence of a year-end true-up makes the fixed bill product a price-based product rather than cost-based. As indicated in the filed testimony and data request responses of the Joint Applicants, this is simply not true. Customers participating in the pilot will receive a fixed bill for an entire year which is based on the expected consumption of the individual customer, multiplied by cost-based tariff rates approved by the Commission. Included in the fixed bill will be an estimate of the fuel adjustment clause and the environmental surcharge, as approved by the Commission. There will be no "market-based" pricing; the fixed bill offers will be prepared under guidelines set forth by this Commission, which, by regulation, incorporates the principles of cost-based rates.

Further, the AG incorrectly asserts that EKPC and the Joint Applicants have considered the fixed bill to be a price-based product, by its reference to an e-mail message included as a part of the Joint Applicants' response to Item 35 of the AG's first set of Data Requests. The AG fails to reference the Joint Applicants' response to the AG's second data request, item 4, wherein the Joint Applicants clarified the context of the use of the term "price-based marketing" in the subject e-mail, and cited several additional reasons why the fixed bill program is not, in fact, price-based.

Finally, as indicated in the testimony and exhibits of Mr. O'Sheasy, the fixed bill product has been in existence for some time in a number of regulatory jurisdictions, all of which are located in the south, southwest or midwest, are not deregulated, and employ the

principles of cost-based rates. The Joint Applicants are requesting an opportunity to embark on a pilot program in Kentucky to determine whether it is a rate alternative that might have benefits for our customers.

**B. The AG’s Concern About the Difficulty of Tracking Losses, If Any, From a Fixed Bill Program is Premature**

While the Joint Applicants acknowledge that the AG may have concerns about isolating the effect of losses under a fixed bill program, the concerns are premature. The Joint Applicants are requesting approval of only a limited pilot program for approximately 1,000 customers, and have indicated, in the response to AG-5, Second Data Request, that we have no intention of attempting to recover revenue losses, if any, as a result of the pilot program. As stated in the testimony of the Joint Applicants, the costs and revenues under the pilot program will be evaluated and reported to the Commission at the conclusion of the pilot. We have also stated in our response to AG-5, Second Data Request, that this issue will be explicitly addressed, if an application for a permanent fixed bill tariff is filed.

**2. The AG comments that the Fixed Bill will provide the utility large margins if actual consumption is lower than expected, but losses can be recovered via rate increases if consumption is higher than expected, resulting in a one-way risk margin. The AG also expresses its concern that the establishment of a special tariff will create a precedent for other utilities, particularly investor-owned utilities, to allow the fixed bill product.**

**The Joint Applicants Respond:**

### **A. The Fixed Bill's Risk Mechanism Is Not One Way**

As stated by Mr. O'Sheasy in his testimony, a risk mechanism has been established which takes into account aspects of the risk of a fixed bill, including weather, usage changes as a result of the mechanism itself and underlying cost risks associated with underestimating the tariff rates and riders, including the level of fuel costs or environmental surcharge. The Joint Applicants agree that if customer use is less than expected, the utility will receive more revenue under a fixed bill compared to a standard bill. However, as indicated in our Application, the next year's fixed bill offer will reflect the lower level of consumption experienced under the fixed bill in the first year, eliminating the possibility of higher margins in the second year. This feature of the program mitigates concerns about inordinate utility margins if consumption is lower than expected. Similarly, if a customer's usage is greater than expected, the Joint Applicants will undercollect compared to the standard tariff. In summary, the proposed fixed bill tariff is not a one way risk mechanism.

### **B. Approval of the Proposed Fixed Bill Pilot Program Would Not Establish Precedent**

The Joint Applicants have proposed only a pilot program. It is an experiment; not a permanent program at this time. It is intended to allow the Joint Applicants to gather information and make a detailed report to the Commission that assesses the viability of the fixed bill concept for electric cooperatives in Kentucky. As a pilot, the Joint Applicants do not accept the idea that its fixed bill proposal would create any precedent that would make it more difficult for the Commission to prevent potential abuse of the fixed bill concept by investor owned utilities in the future. It is anticipated that any permanent program, which may be proposed after the completion of the pilot program, would be fully reviewed by the Commission and appropriate limitations

would be included in any approval of this, or any other, permanent fixed bill programs The Commission has the right and authority to establish and set forth conditions of service under any rate application, based on the merit of that particular application. Approval of this pilot program would in no way limit the ability of the Commission to use its authority to impose appropriate limitations on any similar programs that may be proposed by other utilities in the future.

**3. The AG comments that the fixed bill product encourages “wasteful” consumption, which contradicts the Joint Applicants support of conservation.**

**The Joint Applicants Respond:**

**A. Whether the Fixed Bill Pilot Will Encourage Wasteful Consumption is Not Known**

Without empirical evidence from customers in Kentucky, it is simply unknown whether the consumption by such customers will be “wasteful”. That is why the Joint Applicants have proposed a pilot. As explained by Mr. Bosta and Mr. Lamb, the Joint Applicants will conduct a comprehensive analysis of the consumption changes by fixed bill customers, including the effect on peak demand, which will be compared to a comparable set of data from residential customers who are billed on a standard residential rate. Those results will determine whether the consumption is “wasteful”. The fixed bill concept is designed to give residential consumers the option of monthly rate certainty, not to provide a mechanism for wasteful usage. The Joint Applicants believe that appropriate controls have been included in the program to discourage abuse and remove those consumers who would abuse the fixed bill concept. The results of the pilot program can be used to devise additional limitations, if widespread abuse occurs.

**B. The Only Empirical Evidence Regarding Changes in Peak Demand and Consumption Submitted in the Case Supports Consideration for a Pilot**

Mr. O'Sheasy's testimony states that there has been no statistically significant change in peak demand at Gulf Power Company as a result of their fixed bill pilot, while overall energy consumption has increased. While acknowledging that this may or may not occur in Kentucky, it certainly should offer comfort to all parties that the program does not automatically result in higher peak demand. It is simply another reason to give the pilot program a try.

**CONCLUSION**

The Joint Applicants have proposed a pilot program that will allow residential customers in Kentucky the option of a new, cost-based rate alternative. Fixed bill programs, offering monthly rate certainty to electric consumers, are becoming available in several neighboring states. The proposed pilot program is well-crafted with manageable risks that are not one-sided in order to learn more about whether a new concept like this has merit for cooperatives in Kentucky. It creates no precedent which limits the Commission's authority to set different terms of service in other programs, offers residential customers the choice of monthly rate certainty, and will have no impact on any of the rates of the Joint Applicants. The Joint Applicants hereby request approval to implement the Pilot Program in the spring of 2005.